

Dialogue

Benefits continue to decline as a percentage of premiums

In 2014, fifty-three cents of each \$1 of employers' premium was paid as benefits to the injured worker in California of which 18 cents was spent on providing medical treatment during the recovery period.



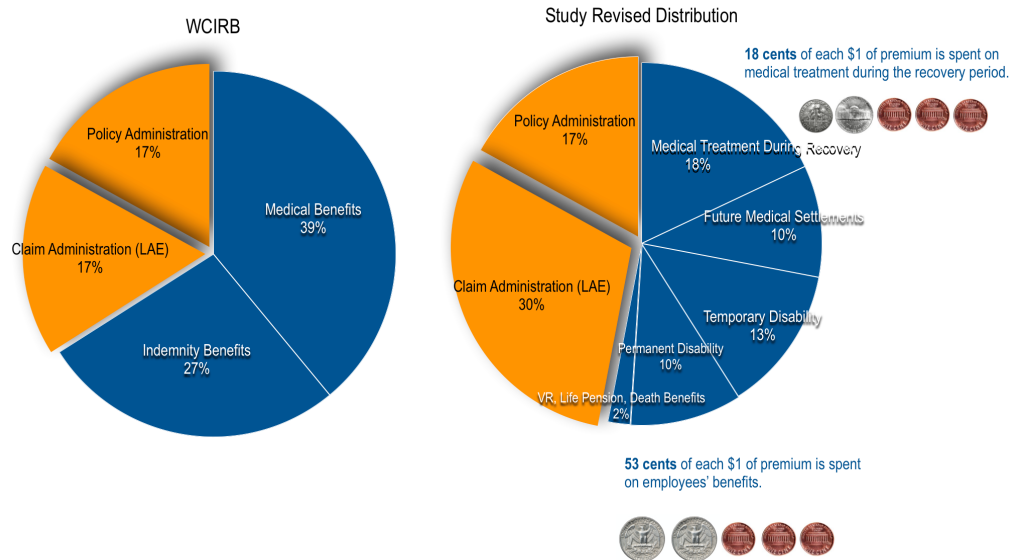
A study using claims data from the Workers' Compensation Insurance Rating Bureau ("WCIRB") focused on claims handling and delivering benefit services, which are often included in costs shown under medical and indemnity benefits, but are not true benefits to the injured worker.

"Can improvements in current claims management practices reduce the excessively high administrative costs for the P&Cs' Workers' Compensation Insurance product?"

The WCIRB reported \$16.9 billion for the cost of the Workers Compensation Insurance product offered by Property and Casualty insurers ("P&C") which included a Loss Adjustment Expense ("LAE") of \$2.9 billion¹. However, transferring costs associated with medical legals, lien settlements and others, from benefits to LAE, and including an estimate for missed medical fraud, lowered benefits and increased LAE to \$5.1 billion.

¹ WCIRB Report on the State of the California Workers' Compensation Insurance System (Rel. July 29, 2015)

Distribution of 2014 P&Cs' California Workers Compensation Insurance Product Costs Totaling \$16.9B



This is an excessively high amount considering 75% to 85% of work-related incidents result in the injured worker returning to work within 1 week. These percentages were recently quoted in an ITL article titled “Are Workers’ Comp Systems Broken?” by Richard Victor. Put into perspective, this computes to an LAE cost of approximately \$6,000 per claim² which by far exceeds the cost of an employee’s benefits for one week. Less than \$1,000 would have been paid for temporary disability (“TD”) based on the maximum 2014 TD rate and adjusting for the TD waiting period. Also, less than \$2,000 would have been paid for medical services including treatments and medications in the majority of these claims.

The P&Cs’ product has exclusivity in providing coverage for statutory workers’ compensation social insurance. Coverage is provided in the form of protection to employers against financial loss caused by paying employees’ benefits. It also provides protection to employees by ensuring they receive their benefits. However, as highlighted, the administrative cost to provide this protection comes at a price of 47 cents for each \$1 of employers’ premiums.

“Wolf” has been cried by P&Cs when asked about reasons for high policy prices citing issues such as the use of opiates/opioids, physician dispensing, compound medications, lack of

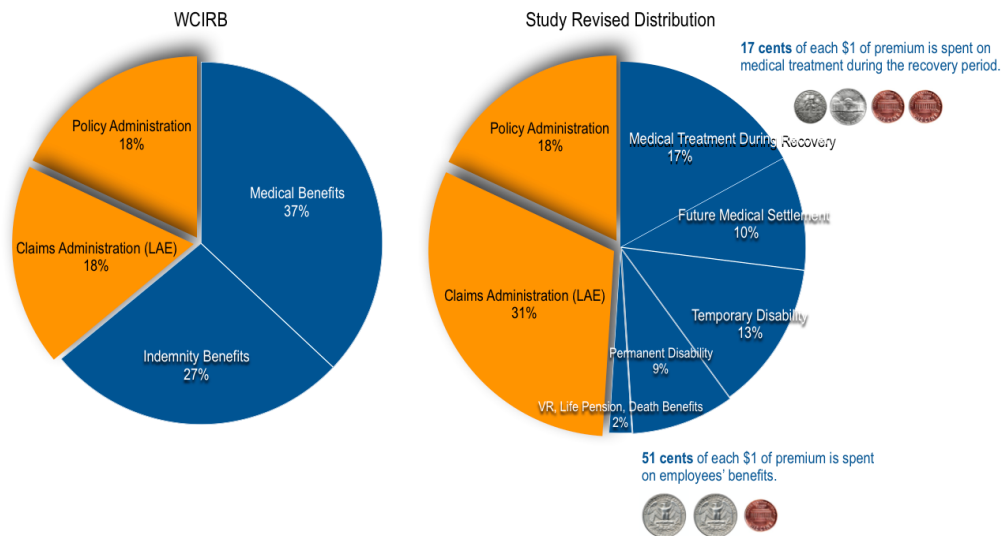
pharmacy formulary, lien claimants, claim litigation, indemnity rates, fraud, high level of regulatory control and more recently, the administration associated with utilization review, processing clinicians’ authorization requests and independent medical/bill review processes. What is constantly being overlooked however, is whether the rise in cost is possibly caused by the P&Cs’ claims management practices.

When discussing the topic of workers’ compensation, many confuse legislated workers’ compensation social insurance with the P&Cs’ workers’ compensation insurance product. This in some ways is understandable, considering its exclusivity in providing coverage. According to insurance historians, this exclusivity came about by default with the enactment of the 1906 Workers’ Compensation Act in England. The Act extended workers’ compensation coverage to employees of private households, such as gardeners, domestic servants and chauffeurs. Property insurance at that time was offered by Fire insurers (called P&Cs today) and were forced to provide coverage for these employees. Prior to the Act of 1906, employers secured protection against exposure from employees’ claims covered by the Employers’ Liability Act of 1880 through a Friendly Society.

Texas is the only state where the purchase of insurance coverage from a P&C is not compulsory. Oklahoma’s enacted Opt-Out

² Based on the WCIRB’s estimate that up to 800,000 claims receive benefits annually.

Distribution of 2015 P&Cs' California Workers Compensation Insurance Product Costs Totalling \$16.8B



statute provides an alternative to their statutory workers' compensation social insurance linked to the P&Cs' insurance product. South Carolina and Tennessee are also considering opt-out statutes. While opt-out has been promoted as a means of lowering the cost of employees' benefits, there has been no discussion or evidence put forward as to how opt-out reduces administrative costs in comparison to the P&Cs' product. As mentioned, benefits only accounted for 53 cents of each \$1 of premium, suggesting if P&Cs focused on reducing their administration costs, premium rates could almost be halved, possibly well below \$2 per \$100 of payroll.

A document titled, "Could 500,000 California Employers Refuse to Purchase Compulsory Workers' Compensation Insurance Coverage Citing P&Cs' Bad Faith?" outlines the calculations and reasonings used in the study to revise benefits and LAE costs. It also explores the four components which generally define claims excellence which are the P&C's culture, resources, operations and procedures and how the State Compensation Insurance Fund and others have applied these components. The infrastructure used to manage claims and deliver employees' benefits was also discussed. The document can be downloaded from the website [managingdisability.com](http://managingdisability.com/dialogue.php) from the Dialogue tab (<http://managingdisability.com/dialogue.php>).

While opt-out is an alternative to the statutory workers' compensation social insurance combined with the P&Cs' product, it should by no means be considered as the only option.

There are other options which can continue to provide coverage for the statutory social insurance without impacting on employees' employability, benefits or the delivery of those benefits as well as focus on reducing administration costs. The bad news for P&Cs is that lawmakers may be forced to consider other options sooner rather than later, which may extend to excluding the P&Cs' product as administrative costs per \$1 of premium continue to increase. For 2015, the WCIRB reported the P&Cs' product cost was \$16.8 billion³. After applying the same adjustments to benefits, administrative costs have now increased to 49 cents with injured workers' benefits having decreased to fifty-one cents for each \$1 of employers' premium.



We Care, We Manage, We Teach

³ WCIRB Report on the State of the California Workers' Compensation Insurance System (Rel. August 2, 2016)